

Air Service Challenges & Opportunities For US Airports



Time To Face Realities -
And, Yes, They Are Tough

Air Service: It's Subject To The Laws of Physics, Too...



Hey, Captain Smith,
let's do a study and find the solution!!!

It went down strictly due to hard, physical realities...

Conditions outside of its control changed factors that no longer permitted this contraption to float. No amount of consulting or Black Magic could have changed these realities. That's exactly the situation in much of the air service picture

Scheduled air service is no different – there are economic realities that can't be reversed.

Yes, That Scraping Sound Is An Iceberg



Howling at the moon won't change economic realities. Neither will social media, "best practices," or another consumer survey.

Communities must start making contingency plans to assure air service access – and that may mean regional cooperation.

Let's Summarize Before We Head To The Lifeboats

- The types of aircraft that are now serving many communities are going away – no question
- There are no aircraft breakthroughs that will result in replacement for "regional" jets. The 50-seat era is over.
- There are no new airlines coming to the rescue – and the LCC growth era is over. Measured growth – and not in rural areas
- Deal with it: at least 100 airports will lose scheduled air service... including many that today have over 100,000 O&D

Let's Look At The Real Trends...



Going out....



Going up....

- **Sheer costs are outrunning ability of markets to support air service locally, so...**
- **The concentration of service IS gravitating to being regionalized**
- **Airline resources = highest & best use only**
- **Airline strategies: maximizing revenues v system costs – shifting to cooperative Alliance strategies**
- **Key metric: revenue flows to/through the alliance is job #1**

The Current State of Rural Air Service

- The physical economic realities of air service have changed
- The cost of flying airplanes across the sky has eclipsed the ability to support it at many communities
- The same economics are causing major airline systems to re-structure
- Air service is no longer a matter of flights at the local airport.
- It's whether whole regions have access to and from the rest of the world –
- Access & Regionalization are the trends of the future
- For many communities, it's time to get off that air service Titanic

It's A Mature Airline Industry



Lovely... but if it doesn't truly access connectivity with the global air transportation system, it's not "air service."

- The "reach" of scheduled air service in North America is shrinking...
- Airlines are not expanding... 2011 traffic was up only @ 1.8%
- Small airliners – 50-seats and less – are going away fast. 65-70 seaters are next.
- The number of airline systems has shrunk materially in the last 20 years
- Tumble to it: Survival in the global economy means access from the rest of the world – not necessarily "local" air service"
- It's not a matter of a route being profitable – it's a matter of profitable **and** compatible with the airline's strategy...

Get with the 21st century... the days of doing a study, giving it to an airline and getting service are over.

The New Metric: Access. Not Volume



**It's Access. Not Passenger Volume
That Brings Economic Growth**

Having travel company service is great – particularly from ultra-efficient Allegiant...

But that's not access to and from the rest of the globe, and that's the new metric of viable airport air service.

- Old metric: enplanements
- New metric (and the only one from an economic impact perspective): Access from the rest of the world...
- Great to have “travel service” flights... but they don't provide access to and from the rest of the globe, which is what “air service” is all about.
- No access, then no investment from China. Or, Chicago, for that matter
- Access is not necessarily at the local airport, anymore...
- Access has been declining in rural America...

Network carriers are cutting capacity – and these reductions will be more pronounced in the 2014 – 2016 period as RJs get culled out...

Regionalization is the name of the game – and it might be at an existing hubsite airport

Air Service Development – A Lot Fewer Phone Calls Needed

1983

Consumers could book & buy on at least 21 large jet operator brands, plus over two dozen independent regional airline brands.

Majors	Regionals
AIR CAL	AIR ILLINOIS
ALASKA	AIR MIDWEST
AMERICA WEST	AIR NEW ORLEANS
AMERICAN	AIR OREGON
CONTINENTAL	AR WISCONSIN
DELTA	ASA
EASTERN	ASPEN
FRONTIER	ATLANTIS
MIDWAY	BAR HARBOR
NEW YORK AIR	BRITT
NORTHWEST	CASCADE
OZARK	CHAPARRAL
PAN AM	COMAIR
PIEDMONT	IMPERIAL
PSA	MALL
REPUBLIC	MESA
SOUTHWEST	METRO
TWA	MIDSTATE
UNITED	NEW AIR
US AIRWAYS	PBA
WESTERN	PLIGRIM
	PRECISION
	RIO
	ROCKY MOUNTAIN
	ROYALE
	SKYWEST

Not a complete list.

2012

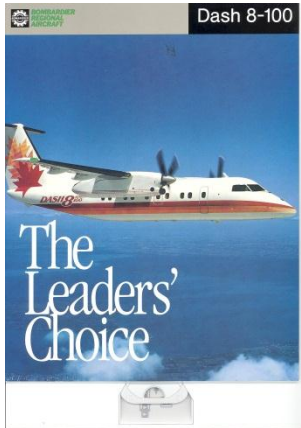
Today, airports can turn to just ten large jet operators, and none of the regionals who were around in 1983 are in the retail airline business.

Majors	Regionals
AIR CAL	
ALASKA	
AMERICA WEST	
AMERICAN	
CONTINENTAL	
DELTA	
EASTERN	
FRONTIER	
MIDWAY	
NEW YORK AIR	
NORTHWEST	
OZARK	
PAN AM	
PIEDMONT	
PSA	
REPUBLIC	
SOUTHWEST	
TWA	
UNITED	
US AIRWAYS	
WESTERN	
Virgin America	
jetBLUE	
SPIRIT	

The Machinery Is Gone...

Entire Fleet Categories Have Disappeared

Dash 8-100



The Leaders' Choice



Beechcraft Commuter C99



This presentation contains detailed information on certain aspects of the performance, specifications, operating costs and standard equipment of the Beechcraft Commuter C99. It is intended to provide information which can be applied in an evaluation of the C99 in relation to actual day-to-day commuter operations. You are encouraged to compare these figures with the aircraft you are now operating or with aircraft you are considering for future operations. Please contact us for any additional information you may need; we are pleased for you to get better acquainted with the Beechcraft Commuter C99. It is made in the U.S.A. by the company listed for its quality.

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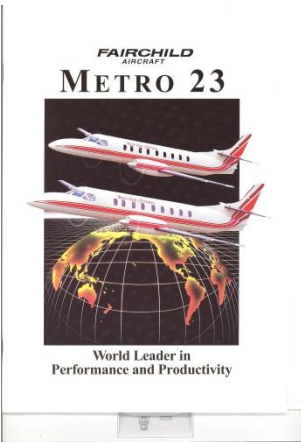
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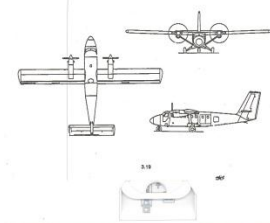
SAAB 340 *plus*




DHC-6 Twin Otter

The main differences between the series are summarized below:

VERSION	119/500	300
ENGINE(S)	PT6A-35	PT6A-37
MAXIMUM TAKEOFF WEIGHT (GROSS WT. USA, 5000)	5850 LBS*	6000 LBS*
TARGET (IF APPLICABLE)	5850 LBS*	6000 LBS*
MAX. CARGO WEIGHT	500 LBS*	500 LBS*
MAX. CREW	4/2	4/2
MAX. PASSENGERS	19	19
MAX. FUEL	445 GALLONS*	445 GALLONS*
WEIGHT (LBS)	11,200	12,000
Maximum "Takeoff" Weight** Landing (G. W. - 15000)	11,200	12,000
WEIGHT (LBS) (Empty)	7,000	7,000
WEIGHT (LBS) (Empty)	68.5	67.8
POWER (LOADED) (Horsepower)	162	176



Not a complete list.

These Are Shrinking

They are already being retired...



Gone already...



Lots of them retired... more are in line for the desert sun



As we speak, in North America, there are close to 200 of these airplanes sitting inactive, retired. They are economically obsolete.

In the 2Q of 2011, some airlines were paying, all-up, almost \$4 per gallon for jet fuel. Spreading this over 50 seats (or less) gets real expensive, real quick.

The Service Bar Is Up...



1990: Beech 1900C - \$750/hour



1995: SF-340 - \$950/hour. Today: @ \$1,800+



2011: CRJ/ERJ - @ \$4,500 - \$4,700/ hour



2020: E-190 - @ \$7,500/hour

Rural & Mid-Size Traffic Is *Falling*

Toss In Declining Capacity, RJ Retirements & Higher Fares ... And plan on this trend continuing... Remember, the main metric for economic air service is access to and from the rest of the globe... Network airline traffic levels are falling at small and mid-size communities across the nation...

Let's look at communities in the southern part of Michigan's Lower Peninsula... Network airline O&D for the full year ending 3Q 2011 v same period ending 2005...

Airport	2005	2011	Chg
MKG	67,651	35,398	-47.7%
GRR	2,013,414	1,916,847	-4.8%
LAN	622,101	230,593	-62.9%
AZO	449,764	213,196	-52.6%
Totals	3,152,930	2,396,034	-24.0%

True, some consumers may be driving to DTW, but it's also down by over 11% for the same period...

Point: airlines are adjusting strategies to the consumer segments that fit operating economics

Regionalization: Example: air access for Central Illinois is excellent... It's just gravitating to a regional point, as service levels decline in smaller airports in the region...

While total demand in the Central Illinois region has fallen by 12%, a substantial shift has occurred to Bloomington-Normal as the "regional" gateway.

Airport	2005	2011	Chg
CMI	239,120	144,183	-39.7%
SPI	172,997	128,274	-25.9%
PIA	468,605	352,578	-24.8%
BMI	449,764	542,594	20.6%
Totals	1,330,486	1,167,629	-12.2%

The impending loss of AirTran at BMI due to acquiring carrier Southwest's high costs has already been addressed by the announced entry of Frontier service to its Denver hub.

Capacity - Reduced

Traffic Demand: These will be driven by the capacity that airline strategies dictate. If a market fits the overall strategy – AND is a better use of resources – it may be considered. Traffic was up only 1.8% in 2011, and currently-scheduled capacity for 2012 is down – *down* – by nearly 2%.



Carrier	Departures				Departing Seats			
	2011	2012	Change	% Change	2011	2012	Change	% Change
AA	1,288,668	1,279,120	-9,548	-0.7%	139,816,569	137,711,788	-2,104,781	-1.5%
B6	248,242	263,501	15,259	6.1%	33,114,600	34,809,850	1,695,250	5.1%
CO	883,355	893,030	9,675	1.1%	83,051,315	82,073,903	-977,412	-1.2%
DL	2,036,549	1,991,255	-45,294	-2.2%	209,075,939	208,073,405	-1,002,534	-0.5%
FL	263,660	222,551	-41,109	-15.6%	31,934,950	27,227,407	-4,707,543	-14.7%
UA	1,179,479	1,179,364	-115	0.0%	103,049,717	102,128,948	-920,769	-0.9%
US	1,168,099	1,156,015	-12,084	-1.0%	106,831,648	109,774,722	2,943,074	2.8%
WN	1,159,034	1,085,225	-73,809	-6.4%	157,903,153	147,895,156	-10,007,997	-6.3%
F9	169,310	126,641	-42,669	-25.2%	17,705,992	15,229,786	-2,476,206	-14.0%
NK	65,945	78,942	12,997	19.7%	9,986,358	12,086,837	2,100,479	21.0%
Total	8,462,341	8,275,644	-186,697	-2.2%	892,470,241	877,011,802	-15,458,439	-1.7%

Point: The term “highest & best use” will be in play...

Key Trends

Major trends to watch



Revenues: Driven by ancillary fees and tight control of capacity – this will continue. Capacity monitoring reduces the potential for at-risk flying.

Expansion: United and Delta are capitalizing on their strengths, but are adding strong, targeted markets that fit specific strategies

“Low Fare Carriers:” The revenue hurdles are going up by the day – and the WN/FL merger does not change that situation. WN has already dropped 15 former AirTran cities due a different operational model and cost structure.

Carrier Strategy To Watch: Spirit. It’s expansion strategy seems to affect WN markets – DFW affects expansion at Love, MSP-ORD affects MSP-MDW... AZA affects PHX.

It's An Issue of Fleets...

All 50-seaters are out of production and are getting older...

Fuel costs on a per-seat basis are getting tougher...

At 35K – 40K hours, they get maintenance-costly

Do the math: By 2010:

CRJ fleets: 21 years old/average

ERJ fleets: 20 years old/average

At 2,000 hours per year, that's over 40K hours

And no replacements... the next cost-hurdle will be 100-seaters (like the E-190) - maybe

Factoid:

Most of the development costs for CRJ and ERJ were borne by the taxpayers of Canada and Brazil when the manufacturers were privatized.

By 2020, The Traffic Requirements Will Be Much Higher

Remember, there will be no small jets – take it to the bank...

And it will be global alliances that will be driving strategy...

Where an airline schedules a \$30 million airplane is much different than a \$15 million unit.

Rough numbers, but indications of a rough future for local air service... Figure what a basic schedule will demand in terms of passengers annually...

Flights Per Day	Equivalent Days	Weeks	Seats/Flt	L/F	Pax Rq
6	6	52	100	85.0%	155,938

Assumes a 98% completion factor

It's About Alliance Territory, Not Local Markets...



“... Don SkyTeam, should we make a move on New Zealand – LAX?...?”

- **Capturing and Defending Revenue Streams.**
Based on each Alliance's strategies, the goal is to capture revenues that build and strengthen the system.
- **Globally, Growth By Adding Members, Not Expanding Incumbents**
The idea is to get regional strength through regional players
- **Territorial**
Alliances will stake out turf - globally
- **Concentration of Pooled Resources**
Today – independent fleets. 2010 – pooled fleets, maintenance, purchasing, standards
- **Focus: Global Flows**
Less ability to serve small & mid-size markets. Less interest, too

Today's Cargo Cult Air Service Approaches



“Okay, guys. If this doesn't work, we'll try a travel bank...”

- **Like:** Another leakage study to find out - yet again - that 70% of the traffic is using another much larger airport 40 minutes away... in some cases, it's not going to change
- **How 'bout:** An unscientific internet survey to find “where people want to fly” - or, worse, “what airline the public wants” – as if there's some airline store out there
- **E Pluribus Dumb:** A Chamber of Commerce “coalition” to let an airline know how much the community needs the airline
- **Goin' Hollywood:** A YouTube video, showing civic leaders imploring the target airline to fly to the community – these have all the impact of a hostage video

Tumble to hard reality: it's a matter of airlines not having airplanes that can serve a smaller markets - period.

Creativity – Some Fun Schemes Already Tried



- A small, unserved airport, 40 minutes away from two low fare carriers, being told they have local service potential for tens of thousands of passengers, with three turboprops a day to a non-hubsite airport. Guess where that went...
- A mid-size airport told that it can be a “hub,” *fed by 9-seat airplanes, even though no carriers bank flights there whatsoever...* The consultant concluded that the airport should hire them to start planning the new airline immediately...
- The Jet America fiasco: Communities persuaded to spend thousands marketing a non-existent airline promising three flights a week to the East Coast... VaporAir
- Communities advised that just getting more “direct” (read: nonstop) flights will instantly spike demand by 40%... (You can’t make this up: *“We’ll find the top four airlines who will fly BUF-MSY nonstop...”*)
- Airports with barely 100,000 enplanements, being told they can “lure a low cost carrier” with a couple \$K in incentives

These are all flim-flam, and just re-arranging the deck chairs, not planning for the future

Okay...



Let's Move Into The Future
Year 2020



Fast Forward To Year 2020

- **Passenger growth slow– up 12% from today - to 517.6 million**
Yes, that's nowhere near historic growth rates, nor within several Zip codes of the FAA
- **Enplanements: up @ 10% to 799.1 million – less connections from rural airports**
- **Fleets: Smallest jet airliner: @ 100 seats**
- **No 50-seat jets are left – they are all run out**
- **“Local air service” not always at the local airport**
- **Regionalization of access**
- **Service determined by potential for revenue capture**

Year 2020 – Get To Know Your New Airlines



Fleets – big iron only

The costs of design and development of a new small-capacity airliner simply are too risky

Point: the enplanement bar will be up – big time.

Competition

Three network carriers – Star, **oneworld**, SkyTeam. A couple of independents – Southwest, JetBlue

Face it – competition will be minimal – the airline business will no longer be one with easy entry or viable return on investment



STAR ALLIANCE

It's A Mathematical Certainty... By 2020 Dozens of Airports Will Lose Service

Small Jet Airliner
Retirements 2011 – 2020

Mergers Have Reduced
Competitive Choices

Code-Share & Frequent
Flyer Program Sharing
Between Alliance
Partners

Major Airline Capacity
Additions – Very Slow &
Anticipatory To Economy

Global Alliance Strategies
Increasingly Focus on
Maximizing Revenue
Flows

Fuel Costs Raise Revenue
Requirement Bar

“Regional Airlines” –
which today are just
leasing aircraft to majors,
shrink dramatically



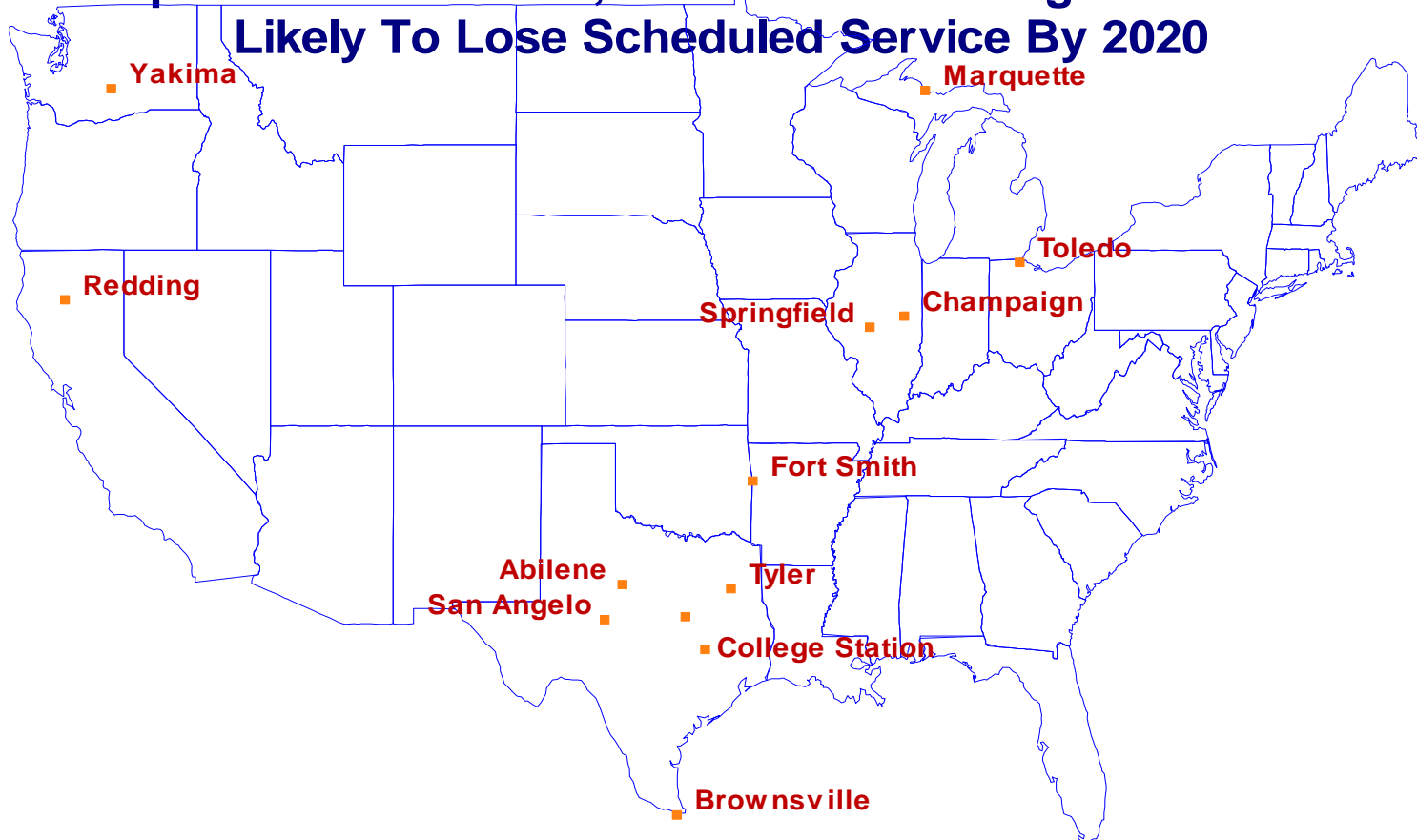
**The New Air
Transportation
System:**

- 100+ Fewer Cities With Local
Air Service**
- Capacity Aimed At Bottom
Line, Not More Passengers...**
- Trend: Less Competition**

“Low Cost Carriers” –
Not Low Cost, Anymore

It's Not Just Very Small Airports: A Few Examples

Airports With Over 50,000 Annual Passengers That Are Likely To Lose Scheduled Service By 2020



These do not include over 100 smaller airports where retirement of small airliners will end service

Yeahbutt... New Airlines Will Pop Up

No, they won't

- **What will they fly? Retired RJs will be run-out and uneconomic at \$3 - \$4 a gallon for jet-A.**
- **Economics make no sense for designers to try new-generation small jets – the R&D cost are prohibitive**
- **There are no viable openings for new airlines trying to fly to East Cupcake. Like inter-urban rail of the early 20th century, it's gone**
- **Low Cost Carriers? Their cost of moving airplanes is too high to “take advantage” of the “opportunities” at Fort Smith or Muskegon, or Champaign/Urbana**
- **The Kicker: Those passengers are not “lost” – they're driving to Grand Rapids, or Bloomington/Normal, or Midland/Odessa – the new regional gateways**

Characteristics Of Potential Regional Gateways

The main decisions on where an airline alliance will place lift comes from the front office – and you can't always count on logical decisions from that area...

But there are factors that make one airport more attractive than others...

- **Strong Industrial Base.** Particularly an international-focused business base: Montgomery... Charleston WV... etc.
- **Anchor Business W/ Big Travel Budget:** Alliances will salivate at getting the travel budget of major employer – State Farm at BMI
- **Surrounded By Smaller Markets Nearby:** This is business, nothing personal. If there's no interest in regional access, your airport has a good a chance as any – as long as its current service is already strong. Bootstrapping isn't going to work. Examples: Grand Rapids. Midland TX
- **Yields:** This is one area where you want to have strong airline fares. The goal is access from the rest of the globe. It that means no cheapo fares, that's the deal. Shreveport: your high fares don't make airlines unhappy. And happy airlines bring service to town

Regional v Metro Peripheral Markets

- Not all traffic will automatically funnel into regional gateways...
- Some markets are stand-alone: Traverse City. Saginaw. Flagstaff.
- There are markets that have local traffic sufficient to maintain strong local service – particularly where local industry is strong and focused – Flint. Lincoln. L.A. Basin.
- Watch population & business trends – Flint got strong access to migration out of Detroit. Toledo did not. It just moved north, not south – nor west, toward Lansing
- The move toward regionalization is driven by a combination of consumer & airline strategies, so...
- Regional planning will facilitate the process – the region can control it or, it can be haphazard or not at all
- The airlines of 2020 will be heavily-dependent on “road hubbing” – markets with strong 4-lane feeder systems will have the advantage

Wrapping Up: So, What Are You Planning For?

- First: all of the financial factors have changed for the airline industry... the air service recruitment techniques of 2005 are now like trying to put a vacuum tube into an iPad. Meeting and schmoozing with airline planners is nice, but now you have to have more than a travel bank and a leakage study
- Identify which category of market you fit into – or can work to fit into – for each alliance
- Note: Assume that individual airline brands will evolve into an alliance identity – US & UA will represent one alliance strategy
- If regional jets got replaced tomorrow with 100 seaters, where would you stand, revenue v cost? Load factors? Hub access.
- Hard analysis: What are the airport alternatives in the region? What are the airline strategies/capture. Are you a potential GRR? Or a Champaign?
- Remember, your economic future depends on access from the rest of the world – and airlines don't give a rip about local sensibilities. The sooner communities work together, the better chance of assuring access in the future

Finally... If You're Planning For The Future, Give Us A Call. We Talk Straight.

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